LETTER OPINION
95-L-35

February 10, 1995

The Honorable Lyle Hanson
House of Representatives
State Capitol
600 E Boulevard Avenue
Bismarck, ND 58505

Dear Representative Hanson:

Thank you for your February 3, 1995, letter in which you ask whether House Bill 1260 is constitutional. In my opinion, if enacted, House Bill 1260 would be constitutional.

The bill proposes to amend N.D.C.C. ?? 15-05-10 and 38-09-18. The former statute concerns oil and gas leases issued by the Board of University and School Lands (Land Board). The latter statute concerns oil and gas leases issued by state agencies and political subdivisions. These statutes require that the leases contain at least a 1/8 royalty. House Bill 1260 proposes to grant state agencies and political subdivisions authority to waive royalty payments until "the costs of drilling the well have been recovered," that is, until the well has "paid out." If this is done, the lease must be revised to provide that upon payout the royalty interest must rise to at least 25 percent. In essence, the bill empowers state agencies and local governments to use their discretion and choose either a traditional royalty or share in the risk of drilling in the hope of greater profit if the well is successful.

I understand that the constitutional question about House Bill 1260 concerns Article IX of the constitution. This article governs lands received at statehood from the federal government. These lands and their proceeds constitute a trust dedicated to the support of schools. N.D. Const. art. IX, ?? 1, 2. This trust is managed by the Land Board. N.D. Const. art. IX, ? 3. Since Article IX is confined to school

lands, other lands managed by the Land Board and lands managed by other state agencies and political subdivisions do not fall within the article. Thus, this analysis of the constitutionality of House Bill 1260 is confined to school trust lands managed by the Land Board.

If House Bill 1260 is enacted, it would be presumed constitutional. Stokka v. Cass County Elec. Coop., 373 N.W.2d 911, 914 (N.D. 1985). The unconstitutionality of a statute must be proven beyond a reasonable doubt. MCI Telecommunications Corp. v. Heitkamp, 523 N.W.2d 548, 552 (N.D. 1994). And at least four justices of the North Dakota Supreme Court must agree that it is unconstitutional. Bismarck Pub. Sch. Dist. No. 1 v. State, 511 N.W.2d 247, 250 (N.D. 1994). It is a heavy burden to prove a statute unconstitutional.

In State ex rel. Sathre v. Board of University and School Lands, 262 N.W. 60, 62 (N.D. 1935), the court considered the constitutionality of a statute similar to House Bill 1260. The statute at issue in Sathre was referred to as Senate Bill 26. It authorized the Land Board

> 'to reduce, scale down, or throw off the interest that may be due upon any land contract or real estate mortgage, or rentals, to the end that justice may be done in dealing with our farmers and to enable the farmers indebted to the Board of University and School Lands to pay their debts and reclaim their property.'

Id. Suit was brought to prevent the Land Board from exercising the power given by Senate Bill 26. Id. The plaintiff argued the Land Board had no authority to accept, in payment of a mortgage, any amount less than the total amount due. Id. at 63. This proposition, it was argued, was supported by section 154 of the Constitution, the present version of which is Article IX, ? 2. Then, as today, this provision, along with other sections in Article IX, imposes a fiduciary duty upon the Land Board in its management of the trust. See 1990 N.D. Op. Att'y Gen. 94, 95-96. Article IX, ? 2 states that "no part of fund shall ever be diverted, even temporarily . . . ."

The Sathre decision examined whether Senate Bill 26 provided for "the diversion of interest or income on funds derived from federal land grants . . . ." 262 N.W. at 65. All five

members of the court concluded that the Legislature could not authorize diversion of the fund to "any objects or purposes other than those for which the grants were made . . . ." Id. at 66. Three justices found Senate Bill 26 did provide for a diversion. Id. But because four justices are needed for a finding of unconstitutionality, Senate Bill 26 was held constitutional. Id.

The reason for the court's conclusion was that the Legislature did not command the Land Board to reduce or forego interest in all cases. Id. at 67. Rather, Senate Bill 26 "merely confers power upon the board so to do." Id. The same is true with Senate Bill 1260. It does not command the Land Board to do anything. It gives the Board discretion to decide whether the trust is better served by taking the traditional royalty or by sharing the risk of drilling a well in the expectation of a greater return to the fund. It is a long-standing rule that the Land Board is "vested with discretion in the performance of its duties." Moses v. Baker, 299 N.W. 315, 316 (N.D. 1941); Fuller v. Board of University and School Lands, 129 N.W. 1029, 1031 (N.D. 1911).

The Sathre opinion implies that if the Land Board were to rely on Senate Bill 26 to forego interest payments that otherwise would be made, then an unconstitutional diversion would occur. 262 N.W. at 67. But this is not what Senate Bill 26 did. It was enacted during the depression, at a time when many lenders, private and public, recognized that their interest would be better served by compromising to reduce unpaid interest. Id. at 67-68. Doing so could result in obtaining "larger payments than they probably would have obtained by standing upon the terms of and enforcing the contract." Id. at 68.

Senate Bill 1260 authorizes the Land Board to decide, in exercising its fiduciary responsibility, whether to stand upon the terms of its original oil and gas lease, or to revise it and hope for a greater royalty upon payout of the well.

The essence of the Sathre decision is that all Senate Bill 26 did was to confer a power upon the Board. Id. at 68-69. This did not, however, change the Land Board's "primary duty" to safeguard the trust fund. Id. at 69. House Bill 1260 confers a power. It does not require the Land Board to exercise that power. Should the Land Board do so, it must carefully weigh all factors and decide, in the exercise of its fiduciary responsibility, what is best for the trust.

If House Bill 1260 is unconstitutional, a similar statute and

a related Land Board policy might also be unconstitutional. The last Legislative Assembly amended N.D.C.C. ? 15-05-10 to authorize the Land Board to reduce royalties "for production from stripper well properties and qualifying secondary recovery and qualifying tertiary recovery projects . . . ." 1993 N.D. Sess. Laws, ch. 159, ? 1. The Board also has a policy to forego its leasehold rights and allow marginally economic wells to temporarily cease production in the hope that the future brings better oil prices. See 1986 N.D. Op. Att'y Gen. 107. While this policy and the 1993 amendment to ? 15-05-10 do not, of course, require the conclusion that House Bill 1260 is constitutional, the fact that the Legislature has enacted a similar statute and that the Board has for sometime implemented a similar policy, is entitled to consideration.

In summary, all House Bill 1260 does is confer a power upon the Land Board. Should the Land Board exercise that power, an unconstitutional diversion of the trust would not necessarily occur. I am sure the Land Board would carefully consider a request to share in the risk of drilling a well. If it would decide to do so, it would not divert the trust fund to another purpose. Rather, it would have exercised its discretion to decide how best to develop and manage the fund.

Sincerely,

Heidi Heitkamp
ATTORNEY GENERAL

cmc/vkk
cc: Rep. Bill Oban
Rep. Ole Aarsvold
Robert Olheiser, Land Commissioner